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Correspondent of The National City Bank of New York

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Economic Conditions
Governmental Finance
United States Securities

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The World Outlook

THE well-informed observer, looking forward into 1923 in an effort to forecast the probable trend of business in the United States, is forced to conclude that the uncertain factor of chief importance is the political situation in Europe. This, of course, is not because our business with Europe is more important than the volume of business at home, for it is small in comparison, but because in some respects our business with Europe vitally affects our domestic business, and domestic conditions by themselves are comparatively stable.

Our relations with Europe are mainly through our exports of agricultural products which in the case of cotton normally amounts to about one-half our production, and in the case of the other staples are large enough to be an important factor in the value of the entire production. The income of our farming population is largely dependent upon Europe's purchases, and the prosperity of all our industries is very much affected by fluctuations in the purchasing power of the farming population.

This European demand under existing conditions is precarious and uncertain. Nobody can say whether it will be maintained or not. It has been well maintained as to foodstuffs to this time, but at declining prices, and by resort to various expedients for means of payment which are temporary and and cannot be relied upon. If European countries cannot pay they cannot buy for very long, and it is evident that the situation in Central Europe is steadily growing more critical.

We have pointed out from month to month ever since the last harvest, that the world situation as to wheat has justified higher prices than have been prevailing, and that the market situation in which wheat for May delivery has been below the spot price is an illogical one. It has indicated a lack of speculative interest, an indisposition to carry wheat to meet future demands which does not exist under normal conditions. If Europe was in position to buy what it wants, prices would be higher, but nobody knows how much it will take. Italy has removed the duty on imports but gone back to the war milling requirements. France has adopted the war milling requirements. Saxony has proposed a 10 per cent admixture of potato-flour with bread-flour and prohibition of the use of bread grains for beer. In German Silesia bread-flour will be rationed. These are symptoms of the pressure to curtail consumption and avoid imports.

Of late, buying for Europe has increased, and the price of wheat is 20 to 25 cents higher than three months ago, but meanwhile the American farmer has sold a large part of his crop, at prices below what the statistical situation under normal conditions would justify, simply because there has been an incalculable risk in carrying wheat over to the late months of the crop year, when the actual scarcity, if any, will appear. And while this situation is more obvious as to wheat than other products, the prices of others are affected in like manner. The poverty and lack of purchasing power of Europe is a constant factor in our markets and a continuing menace to our prosperity. No matter how favorable our domestic conditions may appear, we cannot safely disregard the fact that agriculture must have an outlet in Europe for the usual quantity of its products.

The Reparations Question

The reparations question is the crux of the European situation. There will be no stabilization of foreign currency, no solid basis for trade or confidence, until the reparations question is settled upon a basis which is so far acceptable to the German people as to prompt them to resolutely put their backs into the task of payment. It is possible to make an individual debtor pay, though unwilling, by process of law, providing he owns property which can be seized, sold and applied to that purpose, but society has given up the idea of coercing a debtor who is not possessed of saleable property.

There are only two ways of getting people to work: one is by holding out an inducement, a reward or compensation of some kind that

can be obtained when the work is done. The other is by driving them to it and holding them to it by the power of authority until it is done. The former is the method by which all social progress has been accomplished; the latter has been tried frequently, the last time in Russia, and never been successful. Individuals, much less great bodies of people, cannot be made to work unless they see some eventual advantage to themselves in doing so. In this country we do not attempt to compel coal miners or railroad employes to continue their tasks against their wills, even at pay judicially determined. Work is not effectively done unless the workers put voluntary effort into it.

The reparations payments, to whatever extent they may be possible, must be made with the proceeds of the labor of the German people in the future. The claims cannot be satisfied to any important extent by the seizure of existing property. It would be impossible to dispossess the German people of their lands and fixed property. The productive equipment, even so much as is movable, could not be taken out of the country without making it impossible to collect anything more; it is worth more to the creditors of Germany where it is than it would be anywhere else. To garrison the country would cost a great sum and get nothing, except as the Germans would willingly pay to get rid of the troops. An appeal to that motive, however, would be a shift from the policy of coercion to the policy of bargaining—of seeking to find out what the Germans will undertake to do to clear up the situation, get their affairs in order and be able to build again for the future. Once such a bargain is made upon terms which put the German people in practical unity behind it, the task will be a voluntary one, and the German people will be as anxious to make the payments as the French were when they anticipated the payments upon the $1,000,000,000 indemnity of 1870.

The Present State of Paralysis

There is little reason to doubt that the German people are eager to get such a settlement. It cannot be supposed that any considerable portion of them are happy or contented under existing conditions. Everybody in Germany must know that the country is going rapidly down the road to utter ruin and calamity. If anybody has profited by the degradation of the mark and the ruin that has been imposed upon the creditor class, the number is negligible as a factor of influence in the country. The theory that the policy of inflation and non-payment has been deliberately adopted is untenable, because the consequences to themselves are too terrible and widespread to be voluntarily brought on. The reasonable explanation is that the German people have thought their situation hopeless, that no efforts or sacrifices they could make would enable them to satisfy the terms of the treaty. With such a feeling pervading the country no government can carry through a policy requiring hard labor, patience and sacrifice on the part of the people. The government cannot make the wage earners work 10 hours per day as they did before the war, instead of 8 as they do now. The government of the United States could not do that here, nor could the French government in France. The German executive administration has not been supported upon any policy of taxation or finance that it has proposed. The Reichstag, or legislative body, is split up into numerous parties and factions, so that no legislation has been possible except by compromise or common consent. It may be said, however, that there are other countries in which a lack of harmony in the government has been displayed. When M. Briand and Mr. Lloyd-George came to terms with each other less than a year ago, the French Chamber rejected the policy, putting M. Briand out of office, and since then Lloyd-George has gone the same way. Moreover, even at Washington there are blocs, and entire harmony upon policies does not exist.

The best explanation for the policy of the German government in continuing to print paper money is that it could not stop; it has lacked the strength to put in force any other policy. In the United States months are required for the executive department to make a budget and to pass the necessary legislation to make it effective. A budget amounts to nothing when the currency drops one-half in value within a week. But a government must continue to do business in some way.

Want of Confidence

And so the efforts of individuals to get capital out of the country are best understood, not as a concerted movement to depreciate the German currency or to defeat all reparation payments, but as efforts to get what personal belongings they could out of the ship before it went over the falls toward which it has been steadily drifting.

Mr. Edgar Crammond, a British economist of high standing, made an address before the London Chamber of Commerce recently which is reprinted in the London Times in part, as follows:

Mr. Crammond said that the whole method adopted hitherto for dealing with the problem of reparation appeared to be unsound. There had been twelve conferences; each succeeding conference had drastically reduced the amount declared to be the irreducible minimum at the preceding conference. Each decision of the Allies and their experts had been followed by a further deterioration in the economic condition, and very great differences had developed between the Al-

lies. At the forthcoming Brussels Conference it would be demonstrated that not only could Germany pay nothing, but she must be granted external credits if she was to be saved from utter chaos.

The problem must be dealt with on entirely different lines from those adopted hitherto. The prosperous Germany of 1914 had gone, and in its place they had a very weak and impoverished country, but a country with a great potential capacity of production. The policy must be such as would induce the German people to believe in the economic future of their own country. In order to achieve that the reparations payments must be reduced to such a level as the new Germany could be reasonably expected to pay, and in the second place the German Government must balance its Budget.

A country with the enormous productive power which Germany still possessed could certainly pay a substantial amount, but it would be folly at this stage of the reparations problem to fix a sum which the Allies and the German people would regard as hopeless for her to provide. They could not approve of a policy whereby the whole of Germany's external debt would be cancelled because they would then find themselves in the position, at the end of a few years, of having to pay interest on their own external debt at the rate of forty to forty-five million pounds per annum to the United States, while Germany would be free from any burden of taxation and with her industries developed to a very high point of production.

At a meeting of the Associated Chambers of Commerce of Great Britain recently, Sir Albert Hobson, of Sheffield, was reported as follows:

A revision of the Versailles Treaty seemed inevitable, and if revision had to be made they, as commercial men, wanted to throw their interest on the side of moderation in that revision and of finality when the revision had been made. Without some revision there was no inducement to the German nation to stop the policy of inflation of its paper money. As things were, probably they could not stop it without outside assistance or pressure. He believed the exportable surplus of German goods did not exceed £120,000,000 per annum, and the surplus largely controlled the payment Germany could make. He was opposed to the fantastic idea of keeping Germany under the heel of reparations for forty or fifty years. He favoured an arrangement which permitted a termination in something like twenty years, and 120 millions for that period seemed the utmost they were likely to get.

The sum named annually for 20 years would aggregate about $12,000,000,000. Mr. Arthur Balfour, also of Sheffield, deputy president of the Associated Chambers, while defending France from the charge of being militaristic, declared that German capital had gone abroad because "the conditions in Germany had become impossible." He said that the British army of occupation on the Rhine had cost £56,000,000 sterling and that they had received in reimbursement from Germany £54,000,000 sterling. The report says he believed the only solution of the subject was through a conference of the best industrial men and bankers of the countries concerned, when the whole thing could be analyzed, and it could be seen what was possible and what was not possible.

These are the views of practical men of affairs, whose interests and sympathies lead them to support the allied claims so far as they are realizable.

It is not strange that there should be skepticism as to German protestations of inability to pay, but they are not the moving influence with men like those quoted above. The principal facts of the situation are obvious. It is agreed among competent people that Germany can pay only with the products of her industries and to the extent that she can create an excess of exports over imports. All the evidence available goes to show that she has had no surplus of exports over imports in any year since the war. Her exports to the United States in 1922 according to the import records of this country have been much below what they were in 1913, and probably she has done as well here as anywhere.

Present Conditions

The situation in Germany moves on at a galloping speed. A few weeks ago a new issue of 33,000,000 marks of paper currency in one week was noteworthy, but the pace has since increased to over 100,000,000 in a week. The amount outstanding at the date of the armistice was about 17,500,000,000 marks, and had risen at the end of 1921 to about 100,000,000,000, a sum which in 1922 was multiplied by ten. During the first three months of 1922 the value of the mark was about 200 to the dollar; at the end of the year it was about 9,000 to the dollar. That business goes on after some fashion, simply shows how men will struggle to adapt themselves to conditions seemingly impossible.

These statements and facts are not presented for the purpose of exciting sympathy for Germany. If it was a question of where sympathy was to be placed, consideration would have to be given for the French people who are living in dugouts for the fifth winter since the war. Our purpose is simply to present what we believe to be a correct view of economic conditions in Germany. It is evident that large payments cannot be had from Germany under existing conditions. That country obviously has the productive capacity to pay considerable sums if able to use her capacity, but attempting to get more than the surplus credits she can create in the markets of the world results in getting practically nothing, while prolonging the stagnation of trade in all countries.

Meeting of Premiers

The premiers of Great Britain, France and Italy are meeting in Paris on January 2, 1923, to make another effort to reach an agreement upon a policy to be pursued in the event that Germany fails to make the payment due on January 15th next. That the payment will not be made is a foregone conclusion, as the new German Chancellor has already given out that no more payments will be made under the old arrangement, and that it is absolutely necessary that there shall be a cessation of all payments for a time.

All parties in England are in favor of making new terms to Germany, granting a moratorium for several years, but a moratorium of itself will accomplish little; a reduction of the sum of indemnities is required to a sum that Germany will undertake in earnest to pay.

Once the sum of the obligation is agreed to, all responsible interests in Germany assenting, there is reason to expect that the necessary procedure will be taken for reform of the currency system, balancing the budget and levying the required taxes. A foreign loan probably will be required to assist in stabilizing the currency and foreign exchanges, but with the reparations question settled and the above-mentioned internal reforms under way, such a loan no doubt would be feasible. It goes without saying that Germany has no credit abroad while the reparations question is unsettled, for reparations are a first claim upon her ability to pay anything. There has been no basis for the rumors that American bankers have contemplated offering a German loan in this market.

The relations between the present British and French governments are friendly and cordial. There is mutual confidence and, it is safe to say, not only a desire but intention to maintain the entente. The British appreciate the difficult position of France, burdened with an enormous debt, and obliged to go on adding to it in order to complete the rebuilding of homes in the devastated regions.

The French government strongly disclaims any purpose to permanently hold German territory, does not refuse consent to a moratorium, or to a reduction of the indemnity, but insists that a moratorium must be accompanied by a pledge of tangible assets of some kind, and that it cannot meet its own foreign obligations (to Great Britain and the United States) if obliged to make further concessions to Germany.

The British premier has stated that the Balfour note will not be considered as necessarily binding, and that for the sake of accomplishing a final settlement the British government may consider concessions upon its claims against France. At the same time he protests that Great Britain cannot afford to forgive the debts to itself and at the same time pay its own outstanding obligations.

Although the conditions evidently make it extremely difficult for all the parties to reach an agreement, the necessity for a settlement is so urgent upon all the parties that a supreme effort undoubtedly will be made.

Position of the United States

The position of the United States in regard to the debts running to it is determined at this time by the refunding act. The Commission which is about to enter upon negotiations for the substitution of long-term obligations for the temporary obligations now held by this Government cannot deviate from the terms of the law, nor is it possible for any official representing this Government to enter the council of premiers with the authority to make terms which the premiers of Great Britain, Belgium, France and Italy possess. The American Congress has withheld that power from the executive. The original refunding bill as introduced in behalf of the administration gave power to the Commission, but it was amended to its present form. Senator Smoot, a member of the Commission and Chairman of the Senate Committee on Finance, has said openly in the Senate that in his opinion it is impracticable for this country to attempt the collection of the loans upon the terms of the refunding act. President Harding, commenting upon the Borah resolution for an international conference upon the state of Europe has said that if Congress wishes this Government to take a more active part in dealing with the situation, the first step to be taken is the repeal of the limiting conditions of the refunding act.

The Government at Washington does not believe that its participation is so necessary to a settlement as Europe considers it to be. Its view is that the reparations must be adjusted to Germany's ability to pay; that under no circumstances will any benefit be derived by fixing them above that point, and that it is simple justice for Germany to make reparation as far as she is able to do so. That situation then is complete in itself. The ability or willingness of Germany to pay will not be affected by this country's attitude toward its own debtors. Without holding out any hope that the claims of this country may be modified later, which it cannot do, this Government suggests that there would be more reason in adjusting the claims of the United States to correspond with what its debtors receive from Germany than in adjusting the German payments to correspond with the claims of the United States.

There unquestionably is an important body of public opinion in this country which would like to see the United States represented in the Conference, and have it take the position assumed by the British Government, that for the sake of a final settlement at this time, it would consider the matter of concessions, but as already stated this is at present impracticable.

There is a larger body of opinion in abeyance on the subject, which with no desire to exact the last possible dollar, is not convinced that concessions should be made, at least at this time. It is conservative upon the subject, impressed that nobody knows what the future may have in store, and that time may demonstrate that the debts are not so formidable as they now seem. We are sure that there is a

very general sentiment throughout the country that the debts should not be allowed to impede the recovery of Europe to normal conditions, but that the abilities of the debtor countries to make payments can be judged when recovery has taken place better than now. Of course it is true of this indebtedness.

The Practical Difficulties

The real problem exists in the practical difficulties that attend upon the payment of great sums from one country to another, and in a different currency. It is not simply a question of the ability of the debtor country to collect a given sum from its people by means of taxation. It will collect its revenues in the currency of the country, but it cannot pay the foreign debt in that medium. Moreover, it is as true of the indebtedness to the United States as of the reparations, that payment cannot be made in gold to any important extent but must be made in the products or services of the debtor countries. Upon this point turns the question of their ability to pay, because we ourselves by our national policies are disposed to limit the amounts that may be paid to us in these ways.

Before the war this country had an average annual trade balance in its favor of about $500,000,000, which was practically offset by the so-called invisible charges running against us for services of various kinds rendered by foreign countries. Interest and dividends on foreign investments in this country, charges of foreign shipping, insurance charges and commissions, remittances of foreign-born residents and expenditures of American tourists abroad were the chief items, classed as invisible," as distinguished from merchandise shipments. With the exception of the last two these offsets presumably will be relatively less than formerly. Our private investments abroad probably will offset foreign investments here, and our own shipping will be a larger factor in our trade. Altogether, if we have actually become a creditor country, we must expect to have an adverse balance on merchandise account in order to square the whole account. Our foreign debtors urge that it will be impossible for them to pay unless we consent to take more goods than we sell. Our tariff policy is criticised on this ground.

That view is challenged by many in this country, with various arguments. It is maintained in some quarters that payments upon the debts may be accomplished through triangular transactions, by which the European countries will send goods to South America or tropical countries in payment for products which the latter countries send here, these products being of a kind that we receive free as not competing with ours. This, however, would mean giving up our own aspirations for direct trade with such countries.

If it proves to be difficult for the debtor countries to acquire the credits necessary to meet the debt payments and also make their usual purchases in this country, exchange rates on this country will be high in all other countries, and tend to divert purchases away from our markets. In reply to this argument, it is urged that Europe will be able to borrow largely by means of public flotations in this country, but that cannot help the exchange situation permanently, for it will increase the annual interest payments running this way.

Europe cannot in a complete sense settle its indebtedness to this country by borrowing in this country, although it may be able eventually to settle its indebtedness to the United States government by refunding in the public market here, but that would not relieve the pressure upon the exchange situation. If the balance of payments runs steadily to the United States it will be constantly difficult to find the means of making payments here and the competition abroad for exchange on the United States will put our export business at a disadvantage.

These arguments pro and con are so highly theoretical as not to be convincing to the layman, and even the experts are not agreed, hence the disposition to "wait and see." The sections of the country most directly interested in settlement are the South and West, which supply most of the products that enter foreign markets, and the attitude of those sections no doubt will determine the policy of the country.

General Economic Conditions

Notwithstanding the critical situation over the reparations question and the great disturbance that has been caused politically and economically by the Turkish imbroglio, the general trend of economic development over the past year in Europe and over the world has been toward improvement. Surplus stocks of goods which were congesting the markets have been reduced, international trade has revived in some degree, and exchange rates, except in the cases of countries still operating the printing presses, have moved toward normal. The prices of raw materials, which are prompt to register any change in the activity of industry, are universally higher than a year ago. The political controversies in Europe affect the entire situation, and are everywhere recognized as of the utmost gravity, and yet the feeling in business circles is decidedly more hopeful than a year ago, and there is general belief that with the political questions settled improvement would be rapid.

All of the European countries except Germany have made progress during the past year. Even Austria after sounding the very depths of bankruptcy and despair has had her hopes revived by the action of the League of Nations in securing the co-operation of a group of governments for the establishment of monetary reform. A new bank of issue is being established on a gold basis and a loan provided to take care of the necessities of the government until promised economies and new taxation are made effective in balancing the budget. The printing presses are said to have actually stopped. H. Zimmerman, Burgomaster of Rotterdam, appointed High Commissioner of the League of Nations to supervise the execution of the new scheme, resigned his duties as Burgomaster on December 15 to assume his new responsibilities. At least a serious attempt is being made to put Austria on her feet. Mr. Zimmerman has had an important career in Holland, and is a director in the Holland-America line and the Netherland state railways.

Lord Robert Cecil, speaking in the British Parliament in behalf of the measure to authorize Great Britain's participation in the loan, frankly said that Austria had a very difficult task ahead, saying:

> The moment we get Austria on the road to financial stability we shall have greater difficulty and greater unemployment in Austria probably than she has had for a long time. I do not believe that it can be avoided. As long as a country is content to go on increasing its inflation and diminishing the value of its currency it lives well, because it is living on its capital. The moment it puts an end to that process it lives less well, because it is forced to live on its income, and I am afraid that there is bound to be a period of great difficulty and doubt which can only be solved by the experience as to whether there is sufficient grit in the Austrian people to go through that period for the sake of recovering the solvency of their country.

Poland has brought a large part of her devastated farming districts into cultivation again, and is not only self-supporting as to food but able to export a small quantity. Czecho-Slovakia although suffering at present, from industrial depression resulting from a cause exceptional in Europe, to wit, too rapid appreciation of her currency, has been able to participate with other countries in the stabilization loan to Austria, and gives ample evidence of the stability of her own position.

The countries of southeastern Europe are almost purely agricultural and did not have very good crops in 1922. There is evidence, however, that economic conditions have made improvement in the past year. All of them are encouraging the development of domestic industries, and obtaining more or less foreign capital for that purpose. Jugo-Slavia is building an important railroad to connect the interior with the coast.

In Italy the trade situation has improved and social disorder has been quieted. While the friends of social order may question the policy by which the Fascisti came into power, there is no question that the violent action was the result of a strong popular reaction against socialist and communist activities which threatened to paralyze industry and seize authority. The triumph of the Fascisti, therefore, is indubitable evidence that public sentiment in Italy is very positively against the communist revolution. The revolutionists were beaten at their own game. Industrial and financial conditions have improved and the lire is higher in the foreign exchanges.

The defeats encountered by the socialist element in the agitation for special levies upon capital in Switzerland and Great Britain are further evidence of the reaction throughout Europe against the Russian movement. In Switzerland the vote was about seven to one against the proposition, the number of votes for it exceeding but slightly the number of petitioners initiating it.

Industry in England.

Industrial conditions in England undoubtedly have been better in 1922 than in 1921, although still far from satisfactory. At the present time unemployment doles are being paid by the national government at the rate of $500,000,000 per year, an enormous sum, considering that not only is there nothing received for it but that it is demoralizing in its influence upon the recipients. Nevertheless, British trade was better than in 1921. The monthly Review of the London Joint City and Midland Bank, dated November 30, stated:

> The volume of exports is recovering slowly and is now 70 per cent of the pre-war figure as compared with 60 per cent in the December quarter of 1921. Imports retained for home consumption are also much larger than a year ago, when trade was probably still feeling the effects of the coal stoppage, and it is satisfactory to note that the increase is mainly in raw materials. But, despite these encouraging factors, it is well to realize that there can be no permanent improvement in the volume of our foreign trade until the world's effective demand for goods is increased. With Russia a closed market, Austria and Germany in a state of collapse, the Near East disorganized by war and revolution, and all countries suffering in their internal economy in greater or lesser degree, production and consumption must necessarily, and for a long time to come, be on a reduced scale.

The cotton goods industry had a pronounced revival in the first six months of the year, but in later months relapsed. In the 10 months ended with October exports of cotton piece goods exceeded those of the corresponding period of 1921 by about 55 per cent in quantity, but at that were only 57 per cent of the shipments in the corresponding period of 1913.

The steel industry is doing better, and the outlook for ship-building in 1923 is for more work than in 1922. The coal and iron industries have been stimulated by exports to the

United States. Although this demand has fallen off, the coal industry has continued to gain, the foreign demand from all quarters increasing. The latest reports on production show the rate at 94 per cent of the record year 1913. Steel bars, tin plate and coal have all registered small price increases in the last two months.

Notwithstanding the bad industrial conditions, the British government is steadily reducing its domestic debt, the excess of revenue over expenditures from April 1 to November 25 being about 65,000,000 pounds sterling. Besides that it paid $100,000,000 interest upon its debt to the United States. Sterling exchange made a sensational rise last month, rising to $4.69, from which it reacted, closing the year at about $4.64, compared with about $4.20 a year ago. There is no clear explanation for the rise, but evidently the financial world is not impressed that Great Britain is going to the bow-wows. The gain over the year can be accounted for only by a general improvement in the country's position in international relations.

The Position of France

France is not an industrial country in anything like the degree of the other countries of western Europe. Sixty per cent of the people live on agricultural land. The reconstruction work has made a demand for all labor available for that purpose and kept wages up in a way that has caused some difficulty for other industries. There is practically no unemployment at this time, and economic conditions among the people are generally good. Government finances are in unsatisfactory condition because of the continued necessity to borrow for reconstruction work. M. Lasteyrie, Minister of Finance, in a recent address gave the borrowings in the last four years as follows:

	Francs
1919	51,331,000,000
1920	42,822,000,000
1921	31,120,000,000
1922	21,000,000,000

He explained that so far as the ordinary budget is concerned revenues now cover expenditures, not including interest on the foregoing loans which are for the extraordinary reconstruction work. Revenues are increasing and he hoped to be able to report the total for 1922 as 2,500,000,000 francs in excess of those for 1921. Expenditures have been steadily reduced. The reduction of civil employes in 1922 would be about 50,000. The civil expenditures in 1920 aggregated 11,377,000,000 francs, in 1921, 9,938,000,000 francs and in 1922 would be about 7,023,000,000 francs. Referring to the charge of militarism, he gave the following figures as showing the expenditures upon the national defence for the years named:

	Francs
1919	18,185,000,000
1920	7,648,000,000
1921	6,312,000,000
1922	4,910,000,000

The Minister stated that railroad earnings would be 400,000,000 greater in 1922 than last year. He was very positive in his statement that there would be no inflation of the currency, but a gradual though cautious repayment of obligations to the Bank of France. This will aggregate 1,000,000,000 francs in 1922, causing a retirement of bank notes to about that extent. The needs of the Treasury are financed by offering interest-bearing bonds to the public, which are promptly taken. The interest burden of course increases, and this accounts for the insistence of the French government that Germany must pay enough to finally liquidate these debts.

There is, however, no sign of weakening confidence in the ability of the French nation to go through with the task. The Paris correspondent of the London Economist, writing of this spirit of confidence, said:

> It must be confessed that at present there is a strange undercurrent of optimism pervading this country. Instead of wasting their energies in vain complaints, the whole people are now making a courageous effort to meet their difficulties. The energy and enterprise that has been applied to the restoration of the devastated regions, in spite of an exasperating lack of ready money and of the high price of materials, has been extended to the rest of the country, under many forms. The great scheme for the electrification of the French railways has already reached the commencement of the stage of realism. The same may be said of the nation-wide scheme for the utilization of hydraulic power for the development of electricity to replace steam.

Belgium

Economic conditions in Belgium have improved during the past year. For a time the industries found it difficult to compete with Germany on account of the depreciation of the mark currency, but of late this depreciation has been so rapid and the relations of the mark to other currencies so unstable that German industries has been handicapped rather than aided by it. The Belgian works destroyed during the war have been rebuilt in a substantial and scientific manner, so that their capacity is greater than before. Production is now at about 80 per cent of pre-war capacity.

Holland

Holland has suffered like Belgium from proximity to Germany and the unfair competition of industries that were paying wages in a depreciated currency. Her shipping interest is important and has suffered in the general shrinkage of overseas trade. However, Dutch industry, Dutch traders and Dutch financiers have held their ground and nobody is doubting their ability to do so in the future. The guilder is back practically at par with the dollar.

The Scandinavian Countries

These countries have passed through as severe an experience in the period of deflation as any of the neutrals, owing to the fact that they are all very heavily interested in shipping in proportion to their total investments, and no other industry was carried to such heights or depressed to such depths as shipping. They were closely related to both Germany and Russia, and the collapse in both quarters had disastrous reactions. Finland was in an even more dangerous position by reason of her proximity to Russia, but all of these countries have made substantial progress in recovery, and their exchanges are in much better position. Swedish exchange is now at a slight premium above the dollar.

Russia and Asia

Crops have been better in Russia in 1922 than in 1921, but probably not over 50 per cent of pre-war production. The government has practically abandoned the efforts to extend Communism to the peasants, who comprise about 85 per cent of the population, and extending freedom to small tradesmen and industrialists. It is also offering special inducements to foreign capital and managers to engage in enterprises. It has engaged Professor Cassell, of the University of Sweden, an orthodox economist, as financial adviser, and proposes to establish its monetary system on a metallic base.

India has had a good wheat crop, and is finding a better market for tea, burlap and other prducts, with the result that conditions are better than a year ago.

China is still greatly disturbed by political strife, and the central government is constantly in financial straits, unable to meet the interest on its debts by reason of military expenditures. China's relations with Japan have improved, the latter having withdrawn from Shantung. Business conditions have improved in the past year.

Japan has been proceeding in good faith to carry out her agreements not only with China but under the terms of the International Conference upon naval armaments at Washington, held a year ago. Moreover, she has not only reduced her naval budget materially, but reduced her army by four divisions, and withdrawn her troops from Siberia. Financial and industrial conditions in Japan have improved during the past year, the increased exports of raw silk to the United States, with higher prices for it, being an important factor.

Latin America

The principal products of South America are bringing better prices than a year ago. Wool is doing very much better, and hides, wheat, coffee, sugar, cocoa and nitrate are better. The revenues of the countries are improving, stocks are clearing up, exchange rates are rising, and the situation generally is mending. The cattle industry is depressed, but the grain crop in Argentina now being harvested is one of the largest ever grown. The sugar crop in Cuba now grinding is likely to be a record one, and is bringing a satisfactory price. The island is on the way to full recovery.

Conditions in the United States

As conditions in the United States have been under review from month to month, not much space will be given to this subject at this time. A great recovery has taken place in the past year. The most important feature of it has been the improvement in the prices of agricultural products, tending to restore the normal relationship between these and the products of the other industries. The final estimate by the Department of Agriculture upon the value of the crops of 1922 gives them as $1,800,000,000 over the value for the year 1921. This means so much additional purchasing power to be expended among the other industries, and they are all feeling the benefit of it.

The year ended with the best holiday trade on record and with practically full employment for the available labor supply. The tendency to higher wages and prices shows that the slack has been taken up and this means that the situation is nearly as good as it can be. Some readjustments may be desirable, but when the industries are operating at capacity or to the limit of their labor supply they can do no more, except as methods may be improved. Moreover, when they have reached that stage, there is danger that additional pressure will start a cycle of rising wages and prices, always unhealthful and temporary. After every period of either depression or activity business is likely to swing past the point of balance in the other direction. This should be avoided as far as possible. What is wanted is stability, permanent employment, regular wages, and steady prices.

Aside from the threat of inflation, and with a reservation as to European conditions, the outlook for 1923 is excellent. The principal industries have all the business in sight they need to have to make a prosperous year; the only question is whether it will remain in sight if industrial costs move higher. The margin of profit upon which employers are working, however, is very small. In most of the industries goods cannot be sold today on a replacement basis. Such profits as there are result from making up materials bought at lower prices than are now prevailing. This is

so because certain industrial costs have been maintained at a high level after the buying power of a portion of the consuming public has been reduced. Under such conditions every increase in costs must be passed on to consumers, who for the most part are the wage-earners themselves and the farmers.

This attitude on the part of the wage-workers is due to the common habit of thinking of wages as wholly a matter between employer and employe, and that the higher wages are fixed the better for the employe. Neither assumption is correct, viewing the interests of labor as a whole. When it is known that wages, prices, consumption and employment are all closely related, the fallacy of this idea will be seen. If the compensation of all groups could be raised together, nobody would be benefited, and on the other hand if compensation is raised in a few industries alone, the effect will be to curtail employment in those industries.

The upward tendency of wages and the prospect of another coal strike are features of the 1923 situation prompting the business man to operate with caution.

The Farmer's Position

The Idaho Economic Bulletin, for November, issued by the Department of Economics of the University of Idaho, discusses the whole situation with intelligent comprehension as follows:

> The consequences of this situation are not uniformly advantageous to the economic interests of this state. From the standpoint of the mine operator and mine worker the outlook is good and is likely to continue so for at least six months. From the standpoint of the lumberman and employees in the lumber industry the same is true, barring of course such seasonal fluctuations as appear. From the standpoint of the farmer, on the other hand, the situation is not quite so bright though it need occasion no undue alarm. The farmer's prices in the last analysis are set by foreign demand and foreign ability to pay for his products. If the farmer proposes to limit himself to feeding the people of the United States he might as well go out of business. Over 55 per cent of our exports are agricultural products and raw materials. About 75 per cent of our exports of agricultural products and raw materials go to Europe and about 25 per cent to the rest of the world. Our agricultural exports comprise about 15 per cent of the entire crop value on the farm. In the last fiscal year the quantity of our agricultural exports was greater than it had been the previous year but the value decreased 700 million dollars! Or compare the present figures with those before the war. In 1922 the quantity of grain exported showed an increase well over a hundred per cent above that of 1913; quantity of exports of meats, dairy products and animal fats showed an increase of 36 per cent over 1913, yet the total value of all our agricultural exports showed an increase in the same period of only 13 per cent. At the very moment when the American farmer ought to be taking advantage of the demoralization of Russia to exploit the European market, he finds himself dealing with bankrupt nations unable to purchase his surplus except at bargain prices. If on top of this the price of the things which the farmer must buy begins to mount, even in the face of the reductions in the last year, then the agricultural interests may well look with concern at the sign of re-inflation.

Secretary Wallace, of the Department of Agriculture, names "continued high freight rates and maintenance of industrial wages at near war-time levels" as among the causes of present agricultural distress. On the other hand Secretary Davis of the Department of Labor, congratulates organized labor upon its success in defeating the attempts to reduce wages.

The workers in the textile industries outside of the Southern States have taken only one general reduction from the top wages of the boom period, of 22½ per cent, in December, 1920. They are now moving for its recovery. The average hourly wages of all labor in twenty-three leading industries covered by the investigations of the National Industrial Conference Board were 108 per cent higher in September, 1922, than in July, 1914.

On the other hand, the farmers took an almost perpendicular reduction averaging about 50 per cent from the top level of 1920, from which they have recovered about 17 per cent, and the average purchasing power of the principal farm products in October, 1922, was only 65 per cent of what it was in 1913.

For organized labor to demand the reestablishment of the highest wages of the boom period while buying farm products upon the present level will be an effort to perpetuate an unfair advantage and deprive the farmer of the moderate gain he has made in the past year.

Treasury Report

The annual report of the Secretary of the Treasury, the Hon. Andrew W. Mellon, to the Speaker of the House of Representatives, laid before the latter at the opening of the final session of the present Congress, is a very able document, dealing in a lucid and instructive manner with the Government's numerous financial problems. It begins with a reference to general business so wise and timely that we repeat it herewith:

> Enough forces are operating, therefore, to make us cautious in estimating the prospects for the future and take care lest we build on a false basis. Business in this country can not progress indefinitely without its foreign markets, and undue expansion now, with rising costs and artificial values, would inevitably sow the seeds of reaction and make more difficult the reestablishment of normal relationships abroad. To avoid these pitfalls we depend for the most part on the good sense and foresight of American business. The Treasury, on its part, aims above all to keep its own house in order, in the belief that a sound financial structure here will in the long run afford the best basis for extending needed assistance to Europe and for a healthful revival of domestic business on constructive lines. It has during the year made important progress in readjusting the national finances, and faces the current year with confidence that its fiscal problems can be safely met without disturbance to business and industry. I believe that if in other fields we will proceed with caution and with proper regard for the distressed condition of Europe, it will be possible to maintain our prosperity on a stable basis.

Refunding Operations

The Secretary reviews the debt-paying and refunding achievements by means of which the indebtedness of approximately $7,000,000,000 falling due within about two years, which faced him when he entered the Treasury, has been handled excepting $905,000,000 of 4¾ per cent Victory notes which come due May 20, 1923, and several moderate-sized issues of tax certificates falling due on March 15 and June 15 next. About $1,000,000,000 of the $7,000,000,000 has been paid off out of surplus revenues, and of the remainder $511,000,000 has been converted into 4¼ per cent 25-30 year bonds, and the remainder in the form of Treasury certificates has been spread out with maturities at convenient dates up to September 15, 1926. From now until that time the successive maturities will be handled by refunding operations with such payments as the conditions of the Treasury will permit.

Secretary Mellon is to be congratulated upon the signal success with which he has handled the difficult task that confronted him when he entered upon his office. Every move he has made has proved to be well-conceived and the huge operations have been carried through with a minimum of disturbance to the money market, indeed without noticeable disturbance so far as general business was concerned.

Prospective Revenues

The Secretary reports current gains in the revenues promising to aggregate about $350,000,000, and on the other hand decreased expenditures of about $200,000,000. While the probabilities are that the deficit anticipated at the beginning of the fiscal year will not be entirely overcome, the Secretary does not think it necessary at this time to ask for additional taxes.

The Excessive Income Taxes

The Secretary presents some illuminating facts as to the effects of the high surtaxes upon personal incomes showing that notwithstanding the growth of total revenue from income taxes the proceeds from large incomes have been steadily declining. He estimates that the total revenue from all the surtaxes with respect to the business of the taxable year 1922 will not exceed $350,000,000, which is only about 10 per cent of the total ordinary revenues. He gives the following table showing the decline of taxable incomes of over $300,000:

Year	Number of returns. All classes	Incomes over $300,000	Net income. All classes	Incomes over $300,000	Dividends and interest on investment. All classes	Incomes over $300,000
1916	437,036	1,296	$6,298,577,620	$992,972,986	$3,217,348,030	$706,945,738
1917	3,472,890	1,015	13,652,383,207	731,372,153	3,785,557,955	616,119,892
1918	4,425,114	627	15,924,639,355	401,107,868	3,872,234,935	344,111,461
1919	5,332,760	679	19,859,491,448	440,011,589	3,954,553,925	314,984,884
1920	7,259,944	395	23,735,629,183	246,354,585	4,445,145,223	229,052,039

These figures show that while net incomes of all classes during the period from 1916 to 1920 increased from $6,298,577,620 in 1916, to $23,735,629,183 in 1920, and the number of returns from 437,036 in 1916 to 7,259,944 in 1920, the number of returns of incomes over $300,000 decreased during the same period from 1,296 in 1916, to 395 in 1920, and the amount of incomes over $300,000 from $992,972,986 in 1916 to $246,354,585 in 1920. During this same period investment income of all classes increased, while in incomes over $300,000 investment income shrank from $706,945,738 in 1916 to $229,052,039 in 1920. This indicates an astounding decline in taxable incomes over $300,000 and clearly reflects the tendency of the high surtaxes to reduce taxable income. In this way the surtaxes are gradually defeating their own purpose and the high rates are becoming ineffective because of the steady disappearance of the taxable incomes to which they were intended to apply.

The Secretary does not believe it practicable to enforce the heavy surtaxes. Referring to various methods of avoiding them, he says:

Not all these things can be controlled by law or by regulation, and most of them lead to unnatural and frequently harmful economic results. To reach the evil the thing most necessary is the reduction of the surtax rates themselves, in order to reduce the pressure for avoidance and maintain the revenues derived from the surtax. I believe, therefore, that it would be sound policy, and at the same time most helpful to the general situation, to reduce the surtaxes to a maximum of not over 25 per cent, which would mean a combined maximum, including normal tax and surtax, of not over 33 per cent. Readjusted to this basis, the surtax rates would, in my judgment, accomplish their purpose and yield as large, or larger, revenues to the Government without the unwholesome consequences of the existing rates. The lower rates would at the same time broaden the market for Government securities, and otherwise encourage the development of productive enterprise.

Until such readjustment is made the yield of the higher surtaxes will tend, in the ordinary course of events, to drop toward the vanishing point. The wise course is to reform the surtaxes now while the system still functions and at the same time to close, so far as possible, the gaps which now exist. On this basis the revision can be made without loss of revenue, and, in the long run, with material benefits to the revenues.

It is not very likely that Congress will adopt the Secretary's recommendation. There are too many members who would rather go through the form of levying high taxes on the large incomes, notwithstanding the convincing evidence that the taxes are not paid.

Tax-Exempt Securities

The Secretary says that the most outstanding avenue of escape from the surtax exists in the form of the tax-exempt securities issued by the Federal and State Governments and the political sub-divisions and agencies of the lat-

ter. He says that the effect of these exemptions is to provide a perfect avenue of escape from the Federal surtaxes, especially valuable to the wealthiest investors. He renews his recommendation that Congress adopt and submit to the states the proposed constitutional amendment to stop the further issue of these tax-exempt securities.

The debate upon this proposal so far as it has progressed has indicated that substantial opposition to it exists, and that it may not be practicable to secure ratification by the required number of states. Another development of an interesting character is the denunciation of investors who buy the tax-exempt securities. Congressman Frear in his phillipic against tax-dodgers quotes Secretary Mellon as estimating that $10,000,000,000 has gone into tax-exempt securities to dodge taxes. What the Secretary actually said was that there were estimated to be $10,000,000,000 of tax-exempt securities outstanding; of course, they are all exempt from taxation, whoever owns them, because the laws of the land make them so.

Whatever one's opinion may be of the policy of maintaining the present exemptions, it certainly is a strange situation when citizens cannot respond to the solicitations of their own State and Federal Governments for funds without being subjected to scorn and denunciation. Some 18 states have offered bonds for the purpose of paying soldiers' bonuses, but according to this line of comment nobody should have bought them.

There is nothing clandestine or irregular about the action of the investors, nor are they responsible for the fact that the securities are tax-exempt. The responsibility is with the legislators who not only permit the situation to exist in the case of the government issues, but who go out of their way to create other tax-exempt issues, like the Federal Farm Loan bonds, for the very purpose of attracting this class of investors. They must know that a five per cent bond exempt from taxation is much more attractive to an investor who is subject to the high surtaxes than to an investor who is not subject to the surtaxes. It is scarcely consistent for Congressmen like Mr. Frear, who helped to create the Land Bank System, to denounce the purchasers of the bonds as public enemies.

Corporation Surplus and Stock Dividends

Our discussion of this subject in the last number of this publication has evoked considerable comment, but none of it controverts the essential facts as therein set forth. These, restated briefly, are as follows:

(1) Corporation surplus consists of surplus assets above corporation liabilities, including outstanding capital stock. A surplus is frequently created for a new corporation by issuing the stock at a premium, for instance at $125 for a $100 share of stock. The object in so doing is to provide a margin of working capital in excess of the liabilities and a buffer to protect the legal capital from impairment if losses should occur—in this respect a precaution against emergencies. As an example of paid-in surplus may be mentioned the Brotherhood of Locomotive Engineers' National Bank, of Cleveland, the capital of which was subscribed at $110 per share, thus creating a surplus of $100,000 when the bank began business. Aside from such provisions, surplus is usually created by turning earnings back into the business, or, rather, allowing them to remain, instead of distributing them to stockholders. Earnings thus retained become an indistinguishable part of the operating capital. They increase the earning power of the business and by so doing increase the value of the outstanding stock. The extent to which earnings are thus withheld from distribution usually depends upon the opportunities for enlarging the business. It is a way of providing capital for a growing business without going to the public for more.

Adjusting Capital to Value

(2) In the course of time, where this policy is followed, the assets of the corporation become so disproportionate to the amount of capital stock outstanding that for various reasons, explained in detail in the former article, it becomes desirable to bring them into more appropriate relations. It is common practice to have a share of stock represent $100 of assets, and certificates of stock generally so state. Each share, however, represents a proportionate interest in the entire assets of the corporation, and as surplus accumulates the shares often come to have a value much in excess of $100 each. A stock "dividend" distributes to the stockholders additional shares based on the surplus accumulations, but the effect of this is simply to dilute the value of the old shares. The corporation assets which the stock represents are in no respect changed by increasing the amount of stock. There is no distribution of values from the corporation to the stockholders by means of the stock "dividend." The word dividend in this connection is misleading.

The most important effect of such a stock issue is in transferring capital which has been classed as surplus, and which is under the control of directors and not permanently dedicated to the business, to the form of permanent capital. A board of directors may draw on surplus for cash dividends, but when capi-

tal stock has been issued the assets behind it cannot be distributed except by action of the stockholders.

No Escape from Taxes

(3) The value of the new stock to the stockholders is in the expectation that real dividends out of the earnings of the corporation will be paid upon it, and whenever such payments are made the stockholders must pay all the surtaxes provided by law, according to their respective incomes. Therefore, the supposition that a stock "dividend" accomplishes an evasion of taxes is unfounded.

Let it be clear that under the law as it stands now there can be no conveyance of profits from a corporation to its stockholders without the latter being subject to the taxes levied upon personal incomes.

If the recipient of a stock dividend sells his new stock he is required to account for any proportionate increase in capital value since 1913, when the income tax law went into effect. This would be the case, also, if there was no stock dividend but he was selling his old stock. The stock "dividend" gives him nothing that he did not have before. It only splits up his interest into more shares.

(4) When income has been subjected to taxation once, what remains passes from the category of income to the general status of capital. It cannot properly be taxed again except as all previous accumulations of capital are taxed.

Corporation Taxes

In pointing out that corporations pay a nor mal tax of 12½ per cent upon net income, instead of the normal tax of 4 per cent up to $4,000 and 8 per cent above $4,000 for individuals and partnerships, we should have added that corporations are subject also to a special tax in the form of a levy of $1 per $1,000 on the market value of their outstanding capital stock. In determining "market value," the Government takes into account three considerations, to wit:

(a) The net assets of the corporation;
(b) The quoted market value of the stock, if there have been sufficient transactions to give them credibility;
(c) The capitalized value of net earnings at current rates of return in that line of business.

Governmental practice is to take the highest valuation indicated by these methods. Evidently this tax applies to surplus, for surplus will increase the valuation by any of these methods, and when the surplus is large this tax becomes an important addition to the levies upon corporations which do not apply to individuals and partnerships.

As explained in the former article, if graduated taxes were levied upon corporation incomes as upon personal incomes, the effect would be practically to nullify the whole scheme of graduated taxation, because corporation stocks are held by persons of varying incomes, and largely by persons who are not subject to any of the surtaxes, or to the lower ones only.

Capital Accumulations Increase the Revenue

Any scheme that would force corporations to distribute earnings in order that stockholders might become liable for the personal income surtaxes would not only hamper and restrict the development of industry, but in the long run would reduce rather than increase the tax revenues. The earnings which are added to surplus and used to enlarge the business of the companies have the effect of increasing future earnings, all of which are subject to the 12½ per cent tax and capital stock tax. Finally earnings which are disbursed in dividends are scattered widely and to a considerable extent pay no surtaxes. On the other hand, the values which are accruing to individual shareholders in the form of corporation surpluses, are all bound to come under taxable review sooner or later. A stock distribution, while not a real dividend and therefor not taxable in itself, is a preliminary step to a real dividend, which is taxable.

Moreover there would be a permanent loss to industry by a policy that would force the distribution of corporation earnings into the hands of stockholders. So long as they are in the hands of the corporation they are bound to be used productively, but distributed to the stockholders in comparatively small sums they are likely to be used in considerable part to enlarge living expenses, and never find their way back to productive employment. It must be remembered that there is always need for more capital in industry. The wants of an increasing population can be met only by improvements in the industrial equipment, which mean capital in the form of more equipment. It is unsound public policy to force corporation funds into the pockets of the individual owners.

A Congressional Critic

The Hon. James A. Frear, a Congressman from Wisconsin, in a speech in the House of Representatives, has commented at length upon our discussion of last month. His statements serve very well to illustrate the loose and misleading manner with which this subject is frequently treated. It says:

> The bank justifies $775,000,000 net profit in 10 years on the capitalization of Standard Oil of New Jersey, or 77½ per cent annual net profit on $100,000,000, etc.*

This refers to the statement, publicly made by Mr. A. C. Bedford, of the Standard Oil Com-

* Congressional Record, December 20, page 773.

pany, of New Jersey, that in the ten years ended with 1921 the aggregate profits of the company, before taxes, were the sum stated. He said in the same statement, however, that large as this sum might appear to be, after taxes it yielded an average of only 12.76 per cent upon the company's investment during the period, and that it had been the policy of the company for many years to reinvest in the business all its earnings remaining after the dividends. These statements would naturally suggest to the careful reader that the company's investment was more than $100,000,000. Mr. Teagle, President of the company, in his statement made last month to the Senate Committee on Manufactures, of which Senator La Follette is chairman, stated that the net assets of the Standard Oil Company of New Jersey at the close of 1911 were $292,000,000 odd.

Earning Power in the Physical Properties

Mr. Bedford's statement for 10 years covered the time since the decree of the Supreme Court of the United States dissolving the old Standard Oil organization went into effect. This was in 1911. The business, as is well known, dated back far beyond that. The company by the reinvestment of earnings had built up a large surplus—according to Mr. Teagle's statement, approximately $192,000,000 just after the dissolution. These values existed in the company's properties in excess of the values represented by the company's stock. Of course the earning power of a company is not in its capital stock but in its physical properties, and in this case the earning power was not simply $100,000,000. but nearly three times that.

The company was starting anew after the reorganization. It might have sold off $192,000,000 worth of its properties and distributed the proceeds to its stockholders, and proceeded with as much capital as Mr. Frear gives it credit for possessing. Or it might have been recapitalized at that time by the conversion of surplus, in which case Mr. Frear would not have computed the later profits upon the basis of $100,000,000 capital. It proceeded, however, with an actual investment of $292,000,000.

Since that time its annual dividend distributions, as stated by Mr. Bedford, have not averaged 5 per cent on the invested capital. The remainder of the earnings were reinvested from year to year, and Mr. Bedford has stated the average results computed upon the average amount of net capital employed in the business. Mr. Teagle in his statement referred to above gave the profits for the years 1920 and 1921 and the first six months of 1922 as "$213,720,213, or at the rate of 9.6 per cent per annum on the net assets." This is at a higher rate of annual earnings, but a lower percentage, than the 10-year average, showing how the reinvestment of profits increased the earning power in the later years.

Standard Oil has been an exceptionally successful business over a long term of years, largely owing to the phenomenal development in the supply and uses of oil. Judged by percentage upon the capital employed it has not been as profitable as some of the smaller oil companies, but luck is a large factor in the oil business, and if the profits of all the oil companies could be measured against all the capital that has been invested in the oil business the percentage probably would be lower than the average in other lines of business.

As we have previously said, it is not strange that many people should not understand the complexities of corporation finance, but lawmakers may be fairly expected to inform themselves to speak with some degree of accuracy when addressing the House of Representatives. The public has a right to expect that, and most people, even though unfamiliar with corporation bookkeeping would know that it made a difference in the profits whether a company was operating with only $100,000,000 worth of earning power or with an average for the period of over $500,000,000 worth.

Building by Means of Profits

Perhaps Mr. Frear considers that because this company had only $100,000,000 of stock outstanding it had no right to make profits on more than that capital, no matter how much productive property it actually owned and was employing. This would mean that if two companies started in business with the same capital, and one of them divided all its earnings annually among stockholders while the other restricted its division in order to increase the productive capacity of its works, the latter would have no moral right to earn or ever pay dividends upon its capital accumulations. That would be a violation of the principle upon which all thrift is based. It would mean that companies had no right to use earnings for expansion, and the enforcement of that idea of course would put an end to that policy. A merchant would have no right to use the profits of his business to enlarge that business, or a farmer to use his profits to buy more land, although either might invest in the other's business or elsewhere. As a matter of fact, the industries of the country have been built up mainly out of their own earnings. Let any one read the history of the development of the cotton goods industry in the south or in New England, or of the shoe industry, or the clothing or steel industry, or of any other industry, and, judge of the effects upon industry and employment, and upon prices and the standard of living, of a general rule denying all proprietors the right to expand their business out of profits.

Example of a Great Merchant

There died in Philadelphia a few days ago one of the great merchants of his time. He was respected by all who knew him, and seldom has there been such widespread participation in the tribute paid to the memory of a distinguished man. Mr. Wanamaker began his mercantile career with a capital of $2,000. How could he have made his career if it had not been legitimate to increase his capital out of the earnings of the business? He built up a fortune estimated from $30,000,000 upwards, not in speculation, but by the process of steady, gradual expansion in a highly competitive line of business. His business in Philadelphia was incorporated in 1909 with a capital of $7,500,000, but unquestionably the net value of its tangible assets was much greater than that. This excess was surplus, which it would have been perfectly legitimate to have capitalized by the issue of more stock. Such an issue would in no way have altered the actual value of the assets, or made any difference with the prices of goods sold in the store or the earnings of the business. It would have been purely a matter of bookkeeping and of convenience in distributing the certificates of ownership. If he had incorporated it 30 or 40 years ago and made no change in the capitalization meantime, the increase of stock required to represent the assets in the last year of his life would have been very large.

An Example from the West

Not to take examples exclusively from what Mr. Frear regards as the enemy's country, it is perhaps permissable to take one from the west and among his confreres in Washington. In the career of Senator Arthur Capper of Kansas and the farmers' bloc, there is one of a man who has made a handsome fortune in a comparatively few years, for he is only 57. His first venture in the publishing business is said to have been with an investment of $1,000 which he had saved from his salary as a newspaper reporter, and with which he made the first payment on a newspaper in Topeka. Would anyone venture to argue that his profits should always have been limited to an interest return on that $1,000? He is the reputed owner today of two dailies, six weeklies, three semi-monthlies and two monthlies, several of them agricultural papers of wide circulation and large net earnings. Their aggregate valuation runs into the millions, and as in such cases the big accretions are made in the later years of a man's career, when the increasing earnings double up quickly, the Senator is in a fair way to rank high up among plutocrats. His business of giving information and advice to farmers is also highly competitive. Emerson's immortal saying that if any man could make a mouse trap better than any other the world would beat a path to his door, is illustrated by the millions of farmers who have beaten a path to Editor Capper's door, looking for advice. Here again it is demonstrated that some men do not get richer than other men by charging higher prices, but by giving the public what it wants. It is painful to think that if Senator Capper had incorporated his first investment and capitalized it at cost, then continued to operate his multiplied ventures by means of the same corporation, without increasing the amount of stock until 1922, and had then issued more stock to cover the acquired assets, he probably would have been pilloried in Mr. Frear's list and made ineligible for leadership of the farm bloc.

It is needless to name other examples, but there is scarcely a town in the country which does not have a business that is a leading factor in the community and has been built up by means of surplus earnings. It is impossible to name a man whose name is prominently identified with the development of any great industry whose career has not been made possible by that means. And such careers have been heretofore regarded as creditable to the men achieving them.

Ownership of Standard Oil

The idea that Standard Oil is mainly owned or controlled by one man or family should be disposed of by Mr. Teagle's statement before the La Follette committee. Even before the dissolution there were 6,000 stockholders. He said of the ownership:

Prior to 1911 the stocks of all the companies were held together through their ownership by the Standard Oil Company (New Jersey), which prevented separate ownership from coming about through natural processes of disintegration. The decree, to do away with this condition, directed that the stocks of the subsidiary companies be distributed pro rata among the stockholders of the holding company. While, at the moment of distribution, all the companies had identical stock lists, these processes of disintegration began immediately to operate and have been operating ever since.

As illustrative of this, at the time of distribution the Standard Oil Company (New Jersey) had 6,078 stockholders. Twelve of these held more than one per cent each of the company's outstanding stock and a total of just over fifty per cent of the entire stock. On October 31, 1922, there were 11,013 holders of common stock and nearly 40,000 holders of preferred stock. As of June 30, 1922, only six shareholders held one per cent or more of the company's common stock. These six shareholders own a total of 28.4 per cent of the company's common stock. The largest individual owner of common stock is Mr. John D. Rockefeller, Jr., with 11.4 per cent. Three of the remaining five common stockholders on the list, owning together 10 per cent of the common stock, are philanthropic institutions. It may be of interest to the committee to know that Mr. John D. Rockefeller, Sr., has not been a shareholder in the company since 1920, and that the late Mr. William Rockefeller owned only seven hundred shares at the time of his death.

Furthermore, the company made effective about a year and a half ago a stock acquisition plan under which its employes are becoming stockholders. The number of subscribers under this plan is 11,339 and the number of shares of common stock already allotted to them is 44,636. Before the end of 1925 when

this stock is issued in the names of the individual employes there will be added to the company's stock list on the basis of position today, at least 12,000 to 15,000 common stockholders.

The Soviet Doctrine

Mr. Frear protests that not 1 per cent of the people of this country believe in the Soviet theory and that he does not himself, but possibly he does not have a clear conception of either the Soviet theory or his own. The essential error of the Soviet doctrine is in assuming that the achievements of industrial leaders are of no value to society, and that the fruits of their labors can be appropriated at the will of the majority without any disturbance of the processes of production. They do not understand that the men who have the genius to build up great industrial organizations and properties must have the use of the values they create in order to go on with their work. The more they have to work with the more they accomplish, but if the capital they create is taken from them as fast as created their powers are limited. It is not a mere question of justice to the individuals who furnish leadership; at most they only get their living expenses. The real question is that of free play for their powers in up-building the community.

The Soviet lays all emphasis upon the fact that individuals own the great industries, failing to see that but for these individuals the industries for the most part would not exist, and the further fact that these industries are supplying the wants of the population. They worry lest an individual proprietor will make a profit, even though it is evident that his profits are being used to enlarge an industry and cheapen its products to the public. The modern equipment which has multiplied the productive power of industry many times and advanced the standard of living for the entire population has all been provided out of profits, but the central thought of Sovietism is to abolish profits.

There may be a difference between this view and the ideas of Mr. Frear, but it is so faint in the outlines that anyone who accepts the latter is very likely to accept the former also, particularly if he accepts Mr. Frear's multitudinous misstatements. Sovietism is built upon misunderstanding, and when it comes to knowledge of business affairs, Mr. Frear, to judge by his speeches and writings, has little advantage over the Bolsheviki.

Bond Market in 1922

The peak of bond prices for the year, as shown by the Wall Street Journal's average price of forty bonds, was on September 14, with an average price of 92.12, compared with an average price on January 3, 1922, of 70.22. The latter part of September the bond market reacted from the high level of prices, apparently as a result of an oversupply of new securities, but during the closing months of the year with a falling off in the supply of new issues and a gradually improving investment demand it is understood that dealers' shelves were pretty well cleared.

It is the opinion of many investment dealers that in view of this fact and the large interest, dividend and maturity disbursements which will be available on January 1 the market is in an extremely healthy condition, and that new issues which it is rumored will be placed on the market the early part of 1923 will find a ready market.

The average price of forty bonds reported by the Wall Street Journal as of December 21 was 88.82, as compared with January 3, 1922, of 70.22, and with September 14 of 92.12.

During the year the Liberty bond market was an advancing one from practically the beginning of the year to the end of July. The high price of the year was reached on July 27, when Liberty Fourth 4¼s, due 1938, sold at 101.86. Beginning in August, the market became slightly reactionary, and the same issue declined to approximately 98, followed by a gradual improvement thereafter, with the same issue of Liberty Fourth 4¼s, 1938, selling at approximately 98¾ at the close of the year. During the first six months of the year there was exceptionally heavy buying of Liberty Bonds by corporations, attributed to the fact that the income tax law as now in force makes income from U. S. Government securities totally tax-exempt as far as corporations are concerned.

Following is summary taken from the Commercial and Financial Chronicle of corporate, foreign government and municipal financing for ten months ending October 31, 1922, compared with the same ten months of 1921:

1922	New Capital	Refunding	Total
TEN MONTHS ENDED OCT. 31—			
Corporate—Foreign	81.695.000	———	81,695.000
Domestic	1,969 202,867	675.521.840	2,644.724.707
Foreign Government	382,305,000	15,000.000	397.305.000
Farm Loan Issues	314,540.000	42,000.000	356,540,000
War Finance Corporation	———	———	———
Municipal	962,952,118	10.681.170	973.633,288
Canadian	98,984,534	107,135,000	206,119.534
United States Possessions	27,087,000	———	37.087 000
Total	3,846.766,519	850,338,010	4,697,104,529

1921	New Capital	Refunding	Total
TEN MONTHS ENDED OCT. 31—			
Corporate—Foreign	4,275.000	———	4,275,000
Domestic	1,401.691,601	499.401,580	1,901,093,181
Foreign Government	283.770 000	50,000,000	333,770,000
Farm Loan Issues	109,250.000	———	109,250,000
War Finance Corporation	———	———	———
Municipal	862,232,175	6,380,821	868,612,996
Canadian	65 032.000	———	65,032.000
United States Possessions	25 022,000	———	25.022 000
Total	2,751,272,776	555,782,401	3,307,055,177